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Pandora and Canadian Copyright Royalties

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CBC News reported earlier this week about the lack of availability in Canada of online/mobile streaming services in Canada such as Pandora and Spotify: "Mobile music service rejects Canada, blames fees". As noted in the CBC story:

...in Canada, the idea is barely getting off the ground, and one of the biggest players in the industry is blaming royalties sought by major record labels.

"These rates … are astronomical," Tim Westergren, founder of California-based Pandora wrote in an email to The Canadian Press.

"As long as rights societies take this approach, they will prevent Pandora from launching to Canadian users."

The story lit up Canadian websites and Twitter feeds, cited as evidence that Canadian music industry copyright owners were seeking excessive royalties, thereby keeping out desired services (and, for the record, I personally loved using Pandora during the brief period of time it was available in Canada and would welcome its speedy return).

It strikes me, however, that the story is somewhat more nuanced than that: it should be understood as a story about the collective administration of copyright in Canada, the effects of government intervention in the marketplace and how those two factors impact business negotiating strategies. The words of Tim Westergren are probably best seen as a snapshot of a moment in time in the back-and-forth negotiations between a licensor and licensee - and in this post I'll try to describe what it is about the Canadian copyright licensing milieu which explains the narrative set out in that CBC story.

Before going further, it should be noted that Canada is hardly unique when it comes to Pandora: as the FAQ on the Pandora website notes, Pandora only offers its music streaming service in the United States - so Pandora hasn't been able to obtain the licenses it needs on terms it finds agreeable in *any* country except <strike>Canada</strike> the United States [CORRECTED: 9.26.10]. Additionally, as the CBC story notes, "other [similar] services are willing to pay the fees" - MOG has plans to enter the market soon (and hasn't to date because of Canada's "relatively small population", and Rdio is already here, having entered into agreements with the relevant rights collectives. In other words, read the story long enough and it starts to look like the problem lies less with Canada's copyright licensing scheme than with Pandora's willingness to accede to the rates which are being put on the table in front of it.

And therein lies the crux of this story: Pandora and Re:Sound, one of the copyright collectives from which Pandora needs to obtain a license to stream music in Canada, are still in the midst of negotiations about the royalties which Pandora would be obliged to pay. But, because of the structure

of the Canadian copyright licensing regime, the dynamic at work is not simply two commercial entities negotiating in an open market - it involves two entities negotiating in a situation where one of them has the ability to resort to the enforceable decision of a state entity (the Copyright Board of Canada) if it thinks it can get a higher rate than what the party across the table is willing to <strike>give</strike> agree to [CORRECTED: 9.26.10].

In Canada, there are three sets of rights-holders whose interests are engaged when a service like Pandora proposes to stream music online: rights in the compositions (owned by composers and music publishers), rights in the sound recordings (usually owned by record companies) and rights in the performances contained on the sound recordings (often owned by record companies, though the performers usually retain a right to receive royalties). In order to obtain those rights, Pandora need not track down each individual owner, but rather can obtain a license from a collective which acts on behalf of its members - in the case of online streaming, Pandora would need to deal with SOCAN (for public performance rights in the compositions), CMRRA/SODRAC Inc. (CSI) (for reproduction of the compositions) and Re:Sound (formerly the Neighbouring Rights Collective of Canada) (for public performance of the sound recording and performers' performances) (and potentially AVLA/SOPROQ for reproduction of the sound recording in the event that AVLA/SOPROQ elect to file a tariff). Thus, at least three sets of negotiations are required - while seemingly straight-forward, they are complicated by the fact that collectives in Canada have the ability to have tariffs certified by the Copyright Board of Canada. The certification of a tariff means that the applicable collective no longer needs to enter into individual negotiations with an end-user - they can simply offer the license on the terms set out in the tariff.

Making matters even more complicated is the fact that there are no currently certified tariffs applicable to the online streaming of music in the current year. SOCAN's Tariff 22.A, which covered "online music services" which "deliver[] streams to subscribers", only covered the years 1996-2006. SOCAN's proposed tariffs for subsequent years await certification by the Board. Similarly, the CSI certified tariff for online music services covered only the years 2005-2007 - they also have filed various proposed tariffs for subsequent years (for further details on their most recent tariff proposal applicable to online music services, see here). Re:Sound, however, has never had a certified tariff for online music services - they have recently (July 2010) filed a proposed tariff with the Copyright Board which would cover what the proposed tariff describes as "semi-interactive webcasting" (a term, it should be noted, which does not appear in either the SOCAN or CSI tariffs) - and it is that Re:Sound proposed tariff which raised the eyebrows of the CBC reporter who wrote the Pandora story under discussion. As noted in the CBC story:

[Re:Sound] wants to charge web-based music sites that stream to mobile devices the greater of two figures: 45 per cent of the site's gross revenues in Canada or 7.5-tenths of a cent for every song streamed. While that 45% number certainly seems high on first glance, to understand its significance it has to be put into context: the number is just Re:Sound's "opening bid", so to speak, in a process taking place before the Copyright Board. Re:Sound will almost *certainly* not get a number in the final tariff which is anywhere near what they've requested - but they have every incentive to ask for the highest plausible amount, knowing full well that the number will be countered with a much lower number by interested parties who object to it, and that the Board will in all likelihood end up at a

number somewhere between the opening numbers offered by the participants. It's a bit like a segment on *Pawn Stars*: if you're looking to sell something, go in asking for an outrageous amount in the expectation that Rick is going to come back with a low-ball counter and you'll end up somewhere in the middle. But obtaining a license in Canada is like a really strange version of a negotiation, because if you can't come to a mutually agreeable price, one party gets to go to (what is in effect) a government agency and have them set the price. And that's where Pandora seems to find itself: at a guess, they opened negotiations with Re:Sound, couldn't come to an agreement on what the royalty rate should be, and Re:Sound said something along the lines of "Fine, then we'll have the Copyright Board set the royalty" and started the process by asking for a massive (and likely unsustainable) amount. The CBC story, however, glosses over that entire process. But this isn't a uniquely Canadian problem, and none of this will be a surprise for anyone who has followed Pandora: it was only fairly recently that they were able to come to terms in the United States *for the exact same rights* as those controlled by Re:Sound:

The long, strange saga surrounding webcaster royalty payments is (mercifully) over after a multiyear fight.

Back in 2007, the US government's Copyright Royalty Board set royalty rates for the online streaming of music that many in the business felt were unrealistically high for a nascent market, leading at least one prominent streaming service, Pandora, to threaten to pull the plug. Negotiations over an alternate pricing scheme broke down earlier this year, leaving things looking grim. With a slight nudge, however, the parties returned to the table and today announced an agreement that provides webcasters with a new royalty structure.

The fact that negotiations were even happening took Congressional action. In 2008, Congress passed the Webcaster Settlement Act, which gave the webcasters roughly a year to come to terms with SoundExchange, the entity that collects royalties on behalf of the rightsholders. But the deadline set in that act expired earlier this year, an event that triggered the breakdown of the negotiations.

Pandora founder Tim Westergren tells Ars that the parties were reasonably close to an agreement at that point, but backed away once the deadline passed. Westergren credited a number of factors for getting things back on track, including pressure from the webcasters' audience and some innovative ideas from A2IM, a trade group which represents independent musicians; he also praised Representative Howard Berman (D-CA) for getting the parties an extension on the deadline.

If there were no government presence in the marketplace, it's possible these negotiations would be resolved more quickly - the ability to resort to the binding decision of the Copyright Board means that the parties aren't fully incentivized to conclude negotiations between themselves. Compare the lengthy saga, described above, that Pandora endured in the US with SoundExchange (which levies royalties which are subject to the oversight of the US Copyright Royalty Board, and so is broadly similar to the situation in Canada) with the apparent lack of drama that SoundExchange faced with ASCAP, BMI and SESAC (whose royalties are not subject to the oversight of a government agency). The problem isn't so much that collectives are seeking to maximize the fees they receive (that's not

only rational, but what we would expect any actor in a marketplace to do), the problem is the distorting effect of having a government-sanctioned decision imposed on the parties and the agonizing slowness of those decisions being made. By having negotiations over the royalty rate for Canadian music licenses modulated by the Copyright Board (which, because it is, broadly speaking, a government actor is obliged to observe various due process requirements which end up slowing down the process), we end up with a cumbersome, expensive system which may not be well-placed to respond to the pace of change in a digital world.
